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ESG Trends in 2021: What every in-house lawyer needs to know

CPD Legal Studio

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Today's Agenda

- **What is ESG and why important to in-house counsel?**
- **"E" – Environment considerations** - Climate risk towards Net Zero
- **"S" – Social impact** – the emerging area
- **"G" - Governance** – strategy, regulatory framework, compliance risk and value creation
- Measurement & Evaluation

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Trends in climate risk governance and disclosure

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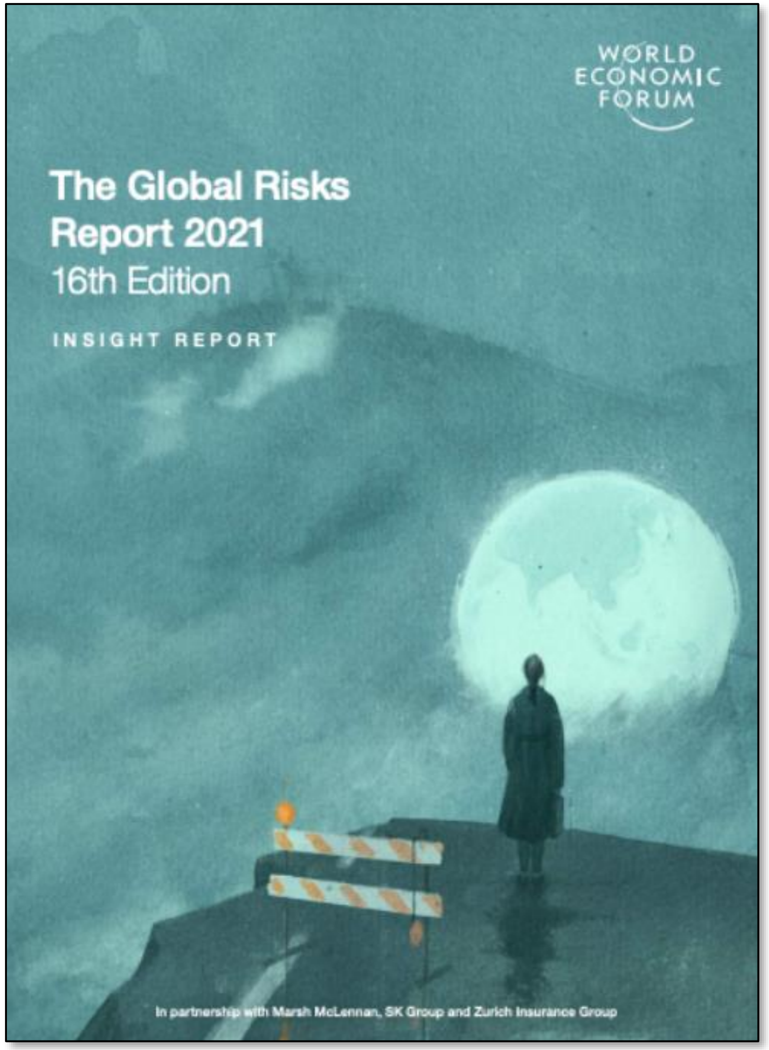
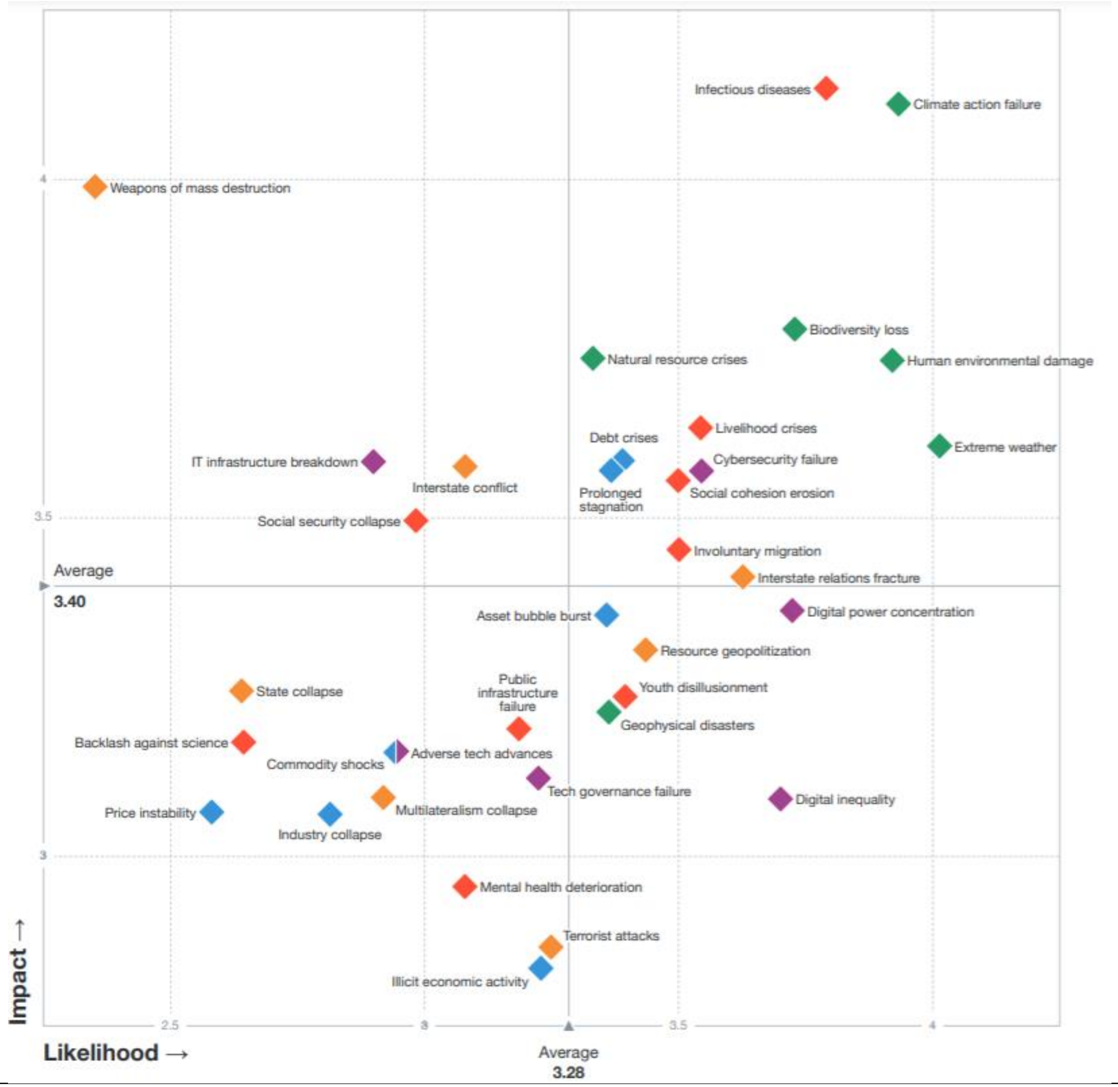
The greatest risk to the global economy is not Covid





Three categories of financial risk associated with climate change

Physical

Acute and gradual onset
To the natural and built environment

Economic transition

The response of governments, capital markets & the real economy

Policy/regulatory, technological & shifts in stakeholder preferences

Liability

Public entity, corporate, and directors/officers

So what are recent developments that will shape climate risk governance in 2021?

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So what are recent developments that will shape climate risk governance in 2021?

The **international regulatory environment** is shifting at an order of magnitude faster than that in Australia

Australian regulators are heightening their scrutiny of annual reports (ASIC), & embarking on stress-testing exercises (APRA)

Investor expectations of boards continue to elevate – despite Covid

Beyond corporate stress-testing, to demand Paris-aligned *strategic plans*

Litigation is the rise – duties, disclosure and development

Focus today:

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#1 - international regulatory environment

A. Net zero by 2050 policies

Required to meet Paris Agreement targets to limit global warming to 'well-below' 2°C above pre-industrial averages

From 10 to 110+ in 2020

Now including EU, UK, Japan, South Korea, California, NY(all 2050) and China (2060)

B. Adjacent policies

Prudential – capital regulatory requirements

Trade – including carbon border tariffs

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#1 - international regulatory environment

C. Accounting Guidance

IFRS has signalled position similar to AASB/AuASB

Consider: what does climate risk mean for asset useful lives, fair values, impairments, provisions for onerous contracts, bad and doubtful debts etc?

November 2020

Effects of climate-related matters on financial statements

This document is intended to support the consistent application of requirements in IFRS® Standards

Climate change is a topic in which investors and other IFRS stakeholders are increasingly interested because of its potential effect on companies' business models, cash flows, financial position and financial performance. Most industries have been, or are likely to be, affected by climate change and efforts to manage its impact. However some companies, industries and activities will be affected more than others.

IFRS Standards do not refer explicitly to climate-related matters. However, companies must consider climate-related matters in applying IFRS Standards when the effect of those matters is material in the context of the financial statements taken as a whole. Information is material[1] if omitting, misstating or obscuring it could reasonably be expected to influence decisions that primary users of financial statements (hereafter, investors) make on the basis of those financial statements, which provide financial information about a specific company. For example, information about how management has considered climate-related matters in preparing a company's financial statements may be material with respect to the most significant judgements and estimates that management has made.

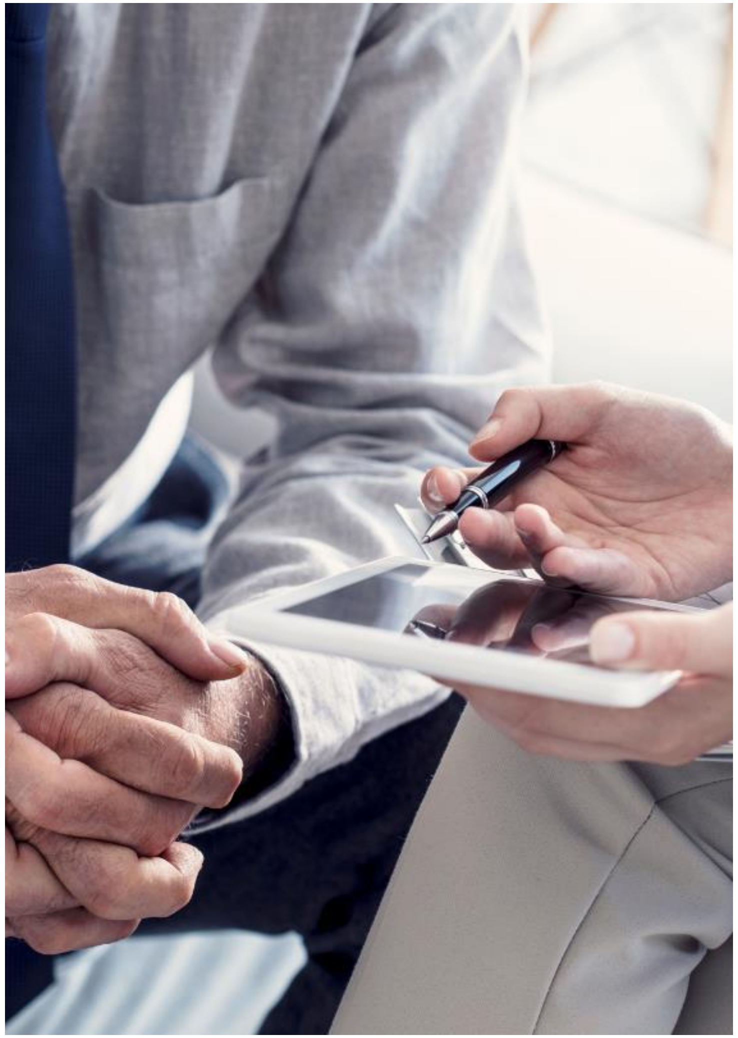
The table below sets out examples illustrating when IFRS Standards may require companies to consider the effects of climate-related matters in applying the principles in a number of Standards. The list is *non-exhaustive*—there could be other instances where climate-related matters are relevant when applying IFRS Standards, for example those on the measurement of defined benefit obligations. Related information can be found in an article by Nick Anderson, member of the International Accounting Standards Board. This educational material complements that article, adding for example specific paragraph references to IFRS requirements to assist those applying IFRS Standards. For purposes of illustration, the descriptions in the table do not always explain the relevant requirements completely; it is therefore important to refer to the requirements in the Standards when preparing financial statements. This document does not address management commentary.

In addition to the specific requirements outlined in the table below, IAS 1 *Presentation of Financial Statements* contains some overarching requirements that could be relevant when considering climate-related matters. For example, paragraph 112 of IAS 1 requires disclosure of information not specifically required by IFRS Standards and not presented elsewhere in the financial statements but that is relevant to an understanding of any of the financial statements. This paragraph, together with paragraph 31 of IAS 1, requires a company to consider whether any material information is missing from its financial statements—ie a company is required to consider whether to provide additional disclosures when compliance with the specific requirements in IFRS Standards is insufficient to enable investors to understand the impact of particular transactions, other events and conditions on the company's financial position and financial performance. Companies will therefore need to consider whether to provide additional disclosures when compliance with the specific requirements in IFRS Standards is insufficient to enable investors to understand the impact of climate-related matters on the company's financial position and financial performance. These overarching requirements in IAS 1 may be especially relevant for companies whose financial position or financial performance is particularly affected by climate-related matters.

1 Companies may find the IFRS Practice Statement 2 *Making Materiality Judgements* useful in assessing whether the effect of climate-related matters is material. The article by Nick Anderson includes further information on making materiality judgements.

IFRS®

Effects of climate-related matters on financial statements | November 2020 | 1



#2 – investor expectations:

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#2 – investor expectations:

*2017 Show us your…***TCFD**

TCFD | TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

#2 – investor expectations:

*2017 Show us your…*TCFD

*2019 Show us your…*stress-testing & scenario planning against **disorderly transition** to a Paris-aligned economy

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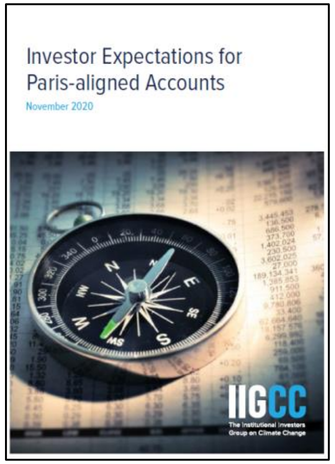
*2017 Show us your…*TCFD

*2019 Show us your…*stress-testing & scenario planning against **disorderly transition** to a Paris-aligned economy

*2021 Show us your…***strategy** aligned with disorderly transition to a Paris-aligned economy, and how this is integrated into your **financial statements**

Climate Action 100+



SCIENCE BASED TARGETS

#3 – strategic litigation:

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Litigation is the rise – duties, disclosure and development

#3 - strategic litigation is increasingly common

Claims against emitters and their boards

Shareholder class actions – overstatement of asset values based on historical assumptions

Yoshikawa v Exxon Mobil (2021)

Government inaction, planning & development approvals

Claims against project proponents and government decision makers Youth Verdict v Waratah Coal (2020) (human rights)

Conservation WA v WA EPA & Woodside (emissions) (2020)

Failure to comply with emissions reductions targets France (2021)

Fund raising disclosures & breach of duties

Prospectus requirements – disclosure of material financial risks O'Donnell v Cth (2020)

Breach of duty to consider climate change McVeigh v REST (settled in 2020)

Advising your board - what does this mean for the legal obligations of directors & officers

The standard of due care and diligence continues to rise, as do minimum requirements for disclosure (misleading disclosure)

At what point does the standard of care *require* consideration of TCFD compliance, net zero strategic pathway?

Consider climate change at a strategic (not tactical) level

Oversight – how robust are the variables & assumptions being applied in your strategic plans and valuation inputs?

3 key takeaways

Key learning

Key qu's & actions

1

This is a foreseeable & material financial risk (& opportunity)

How do we continue to thrive in the transition to net zero?

How do we build capacity - from the board down?

How are climate issues integrated across our business? What is an appropriate governance & risk management structure?

How do we assess relevant risks (&opportunities)?

2

Past experience is not representative of future risk

Does our strategy & planning embed stress-testing & scenario planning on a forward-looking basis?

Taskforce on Climate-related Financial Disclosures

3

Risks (& opportunities) are accelerating

Near the start of the journey: what do we need to do to reach minimum standards –fast? *What are the key drivers of climate-related risk & opportunity? How do they impact on us? What should we set as initial emissions reduction targets – starting within business fence-lines?*

If well progressed: how do we reach/maintain best practice? *Science-based Targets, up- and down-stream, full life-cycle, contracts, sustainable finance?*

Trends in environmental social impact & governance in 2021

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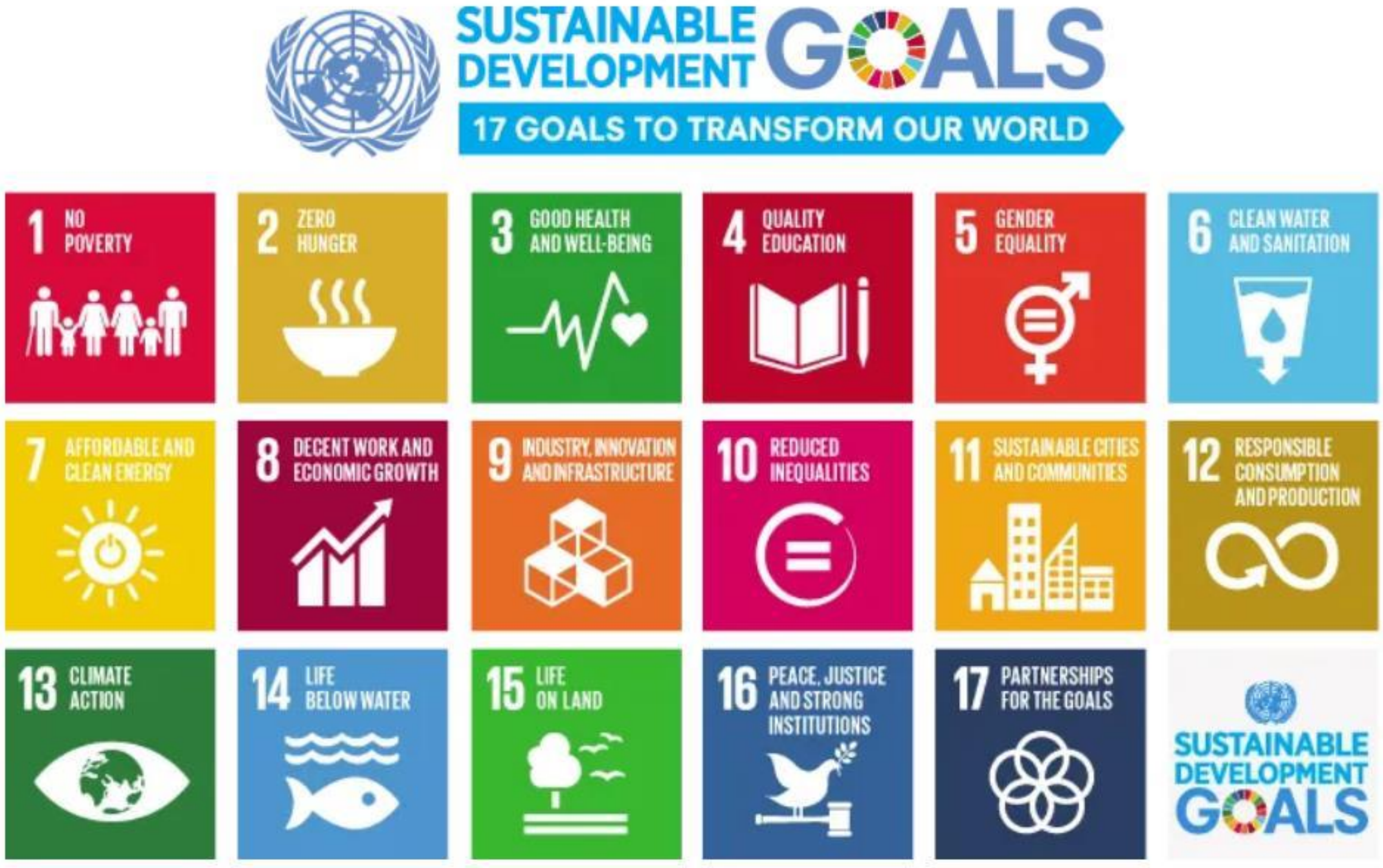
SDGs – the year of biodiversity?



Source: TriplePundit

What does the 'S' in ESG look like?

More like this…

The New York Times

Why You Should Care That Boohoo Is Making Headlines This Week

Boohoo was one of the fastest-growing retailers in Britain. Now the company is in trouble after revelations about working conditions in supplier factories.

How corporate Australia is tackling the mental health crisis

Private Equity Firm TPG Plans to Raise Second Social Impact Fund

'The status quo is unacceptable': Walmart will stop selling some ammunition and exit the handgun market

…less like this

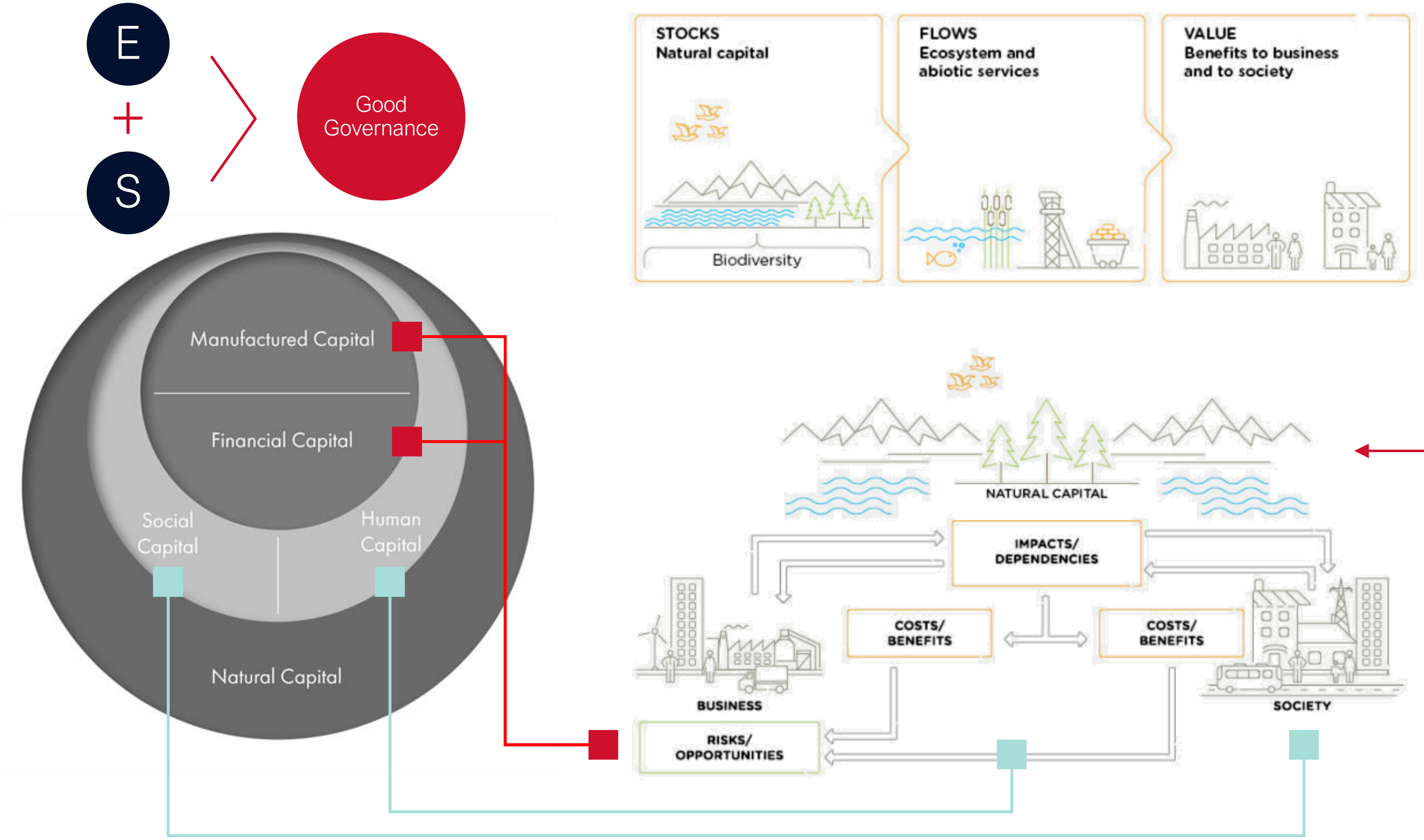
How did CEO pay get to 500 times the wages of ordinary workers?

Target reveals $9 million in staff underpayments in latest wage theft scandal at Wesfarmers

Banking royal commission: Predatory practices, exploitation of Indigenous Australians revealed

Australian CEO bonuses at near record highs despite royal commission

Corporate Governance



Source: **Forum for the Future and the Natural Capital Coalition**

Elements of Governance ESG

Abandoning shareholder primacy – governance and stakeholder and supply chain (human capital, people)

Ensuring balance between shareholder return and social responsibility (CSR)

Transparency via adherence to disclosure frameworks

How have ESG Principles manifested themselves?

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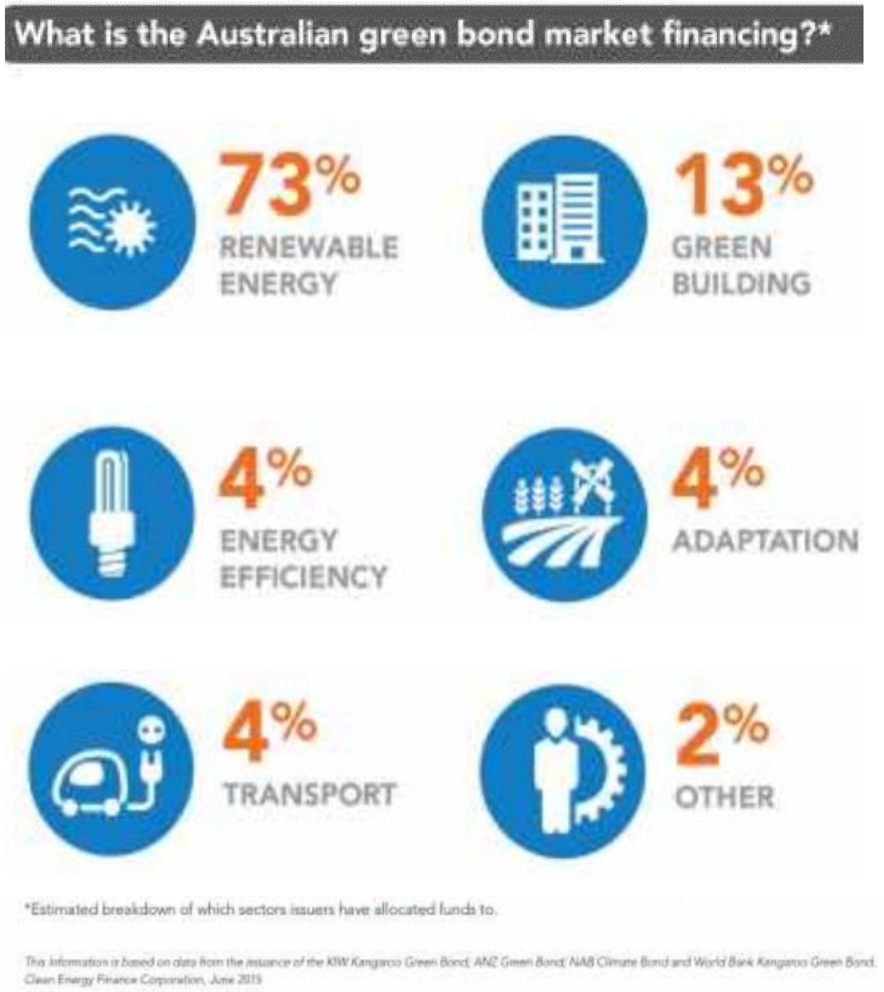
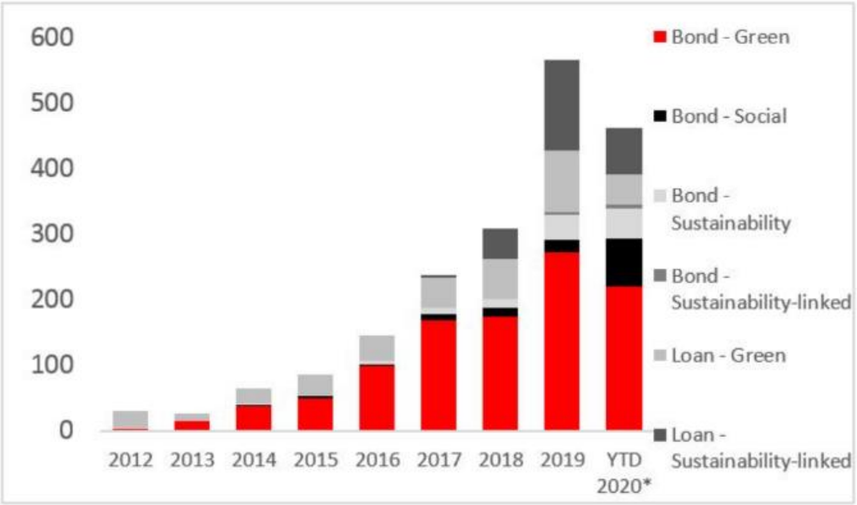
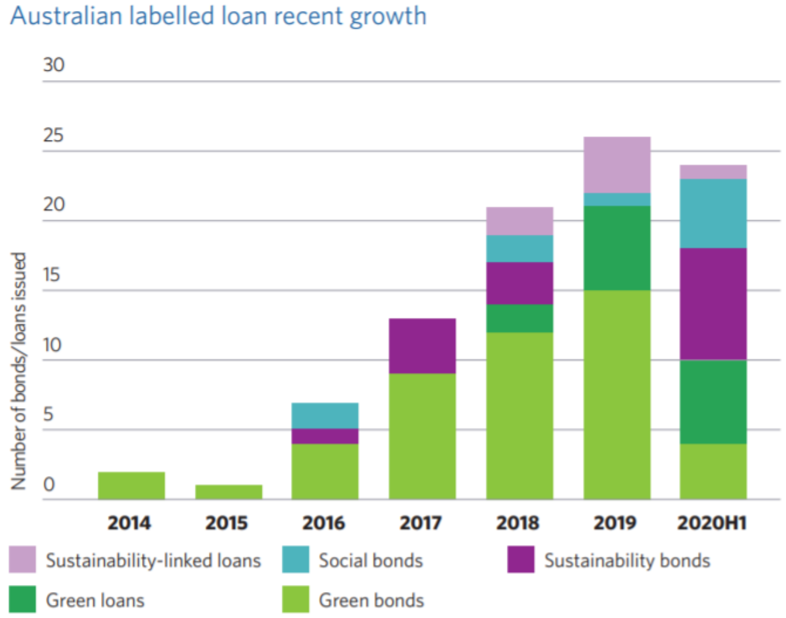
Sustainable finance

Sustainable finance global / Australian market

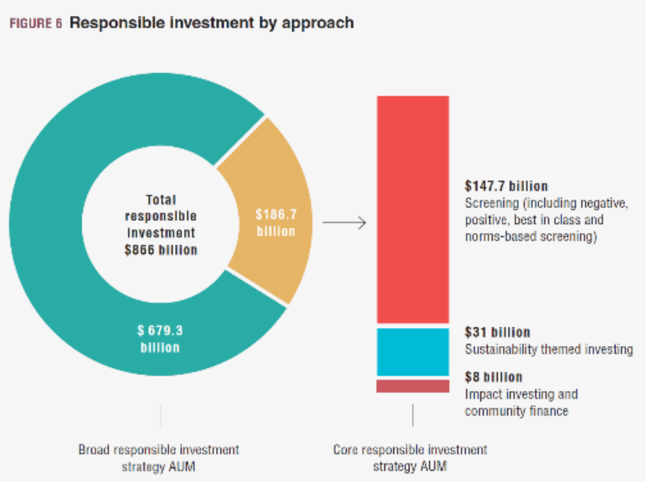


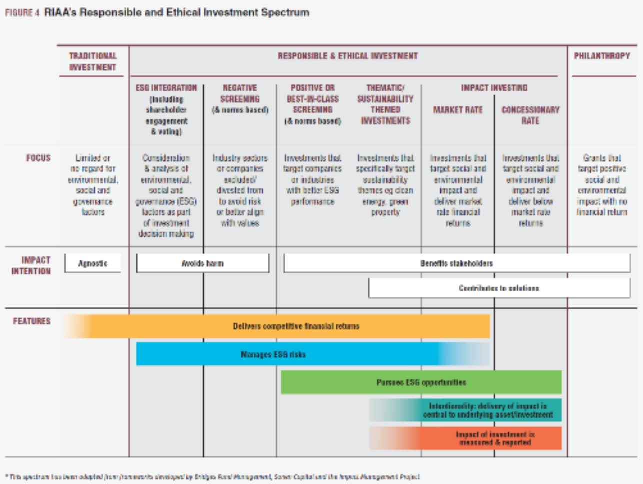


Source: BloombergNEF Sustainable Debt Tool

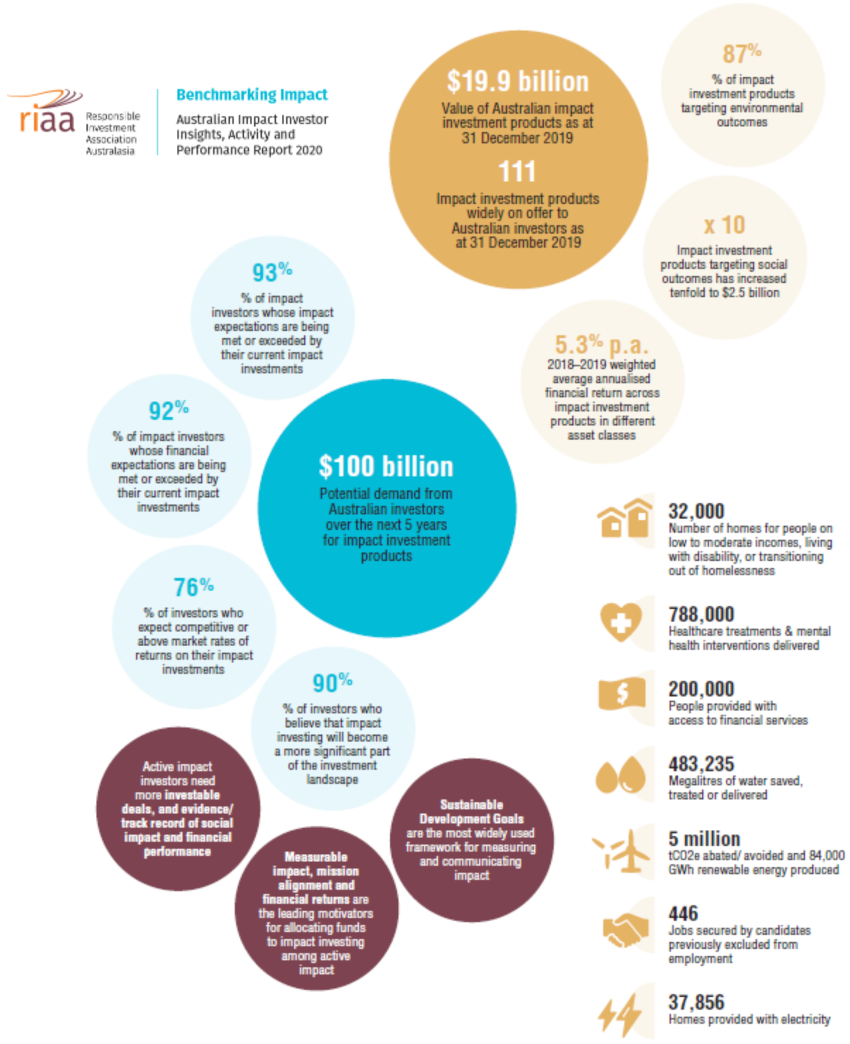


Capital for purpose – Responsible investment





Source: **Responsible Investment Association Australia 2018 report**

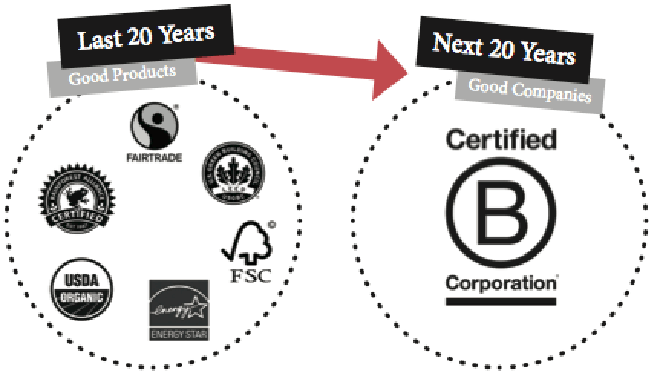


Source: **Environmental Finance: Sustainable Bonds Insight 2019**

MinterEllison's Social Impact Focus

"B Corp is to business what Fair Trade certification is to coffee or USDA Organic certification is to milk. B Corps are for-profit companies certified by the nonprofit B Lab to meet rigorous standards of social and environmental performance, accountability, and transparency."

www.bcorporation.net



TWO GOOD CO.

CHARCOAL LANE

A social enterprise of MISSION AUSTRALIA

THE GOODBOX

Vanguard

LAUNDRY SERVICES

"Findings continue to indicate that many staff experience physical and mental health improvements, and increased levels of social engagement and financial independence. These effects are particularly apparent in the first 12 months. The changes appear to stabilise after the first year, as staff prepare to transition into the open jobs market with support from our Careers Team."

Source: **Social Traders**

Benchmarking ESG

Despite the lack of a standardised body, private actors, independent bodies and government organisations have taken it upon themselves to benchmark ESG

Traditional measures are also useful – Credit Rating Agencies are joining the fray

What you can do – ESG integration

Environmental

E

Social

S

Governance

G

Contact

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